



A REPORT
TO THE
MONTANA
LEGISLATURE

FINANCIAL-COMPLIANCE AUDIT

Office of the Secretary of State

*For the Two Fiscal Years Ended
June 30, 2016*

DECEMBER 2016

LEGISLATIVE AUDIT
DIVISION

16-19

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§5-13-202(2), MCA

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FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Legislative Audit Division to determine whether an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) licenses.

The Single Audit Act Amendments of 1996 and the Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards require the auditor to issue certain financial, internal control, and compliance reports in addition to those reports required by Government Auditing Standards. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2015, was issued March 29, 2016. The Single Audit Report for the two fiscal years ended June 30, 2017, will be issued by March 31, 2018. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
Room 277, State Capitol
P.O. Box 200802
Helena, MT 59620-0802

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Room 160, State Capitol
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LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel



Deputy Legislative Auditors:
Cindy Jorgenson
Joe Murray

December 2016

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report for the Office of the Secretary of State (office) for the two fiscal years ended June 30, 2016. This report does not include any recommendations. We issued unmodified opinions on five of the office's financial schedules. We issued a qualified opinion on the Schedule of Changes in Fund Equity for fiscal year 2015.

Our audit effort focused on charges for services revenue, personal services, contracted services expenditures, and construction work in progress. We audited this activity through sampling, analytical procedures, and testing significant internal controls.

The office's written response to the audit is included in the audit report on page C-1. We would like to thank the secretary and her staff for their cooperation and assistance throughout the audit.

Respectfully submitted,

/s/ Angus Maciver

Angus Maciver
Legislative Auditor

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ELECTED, APPOINTED, AND ADMINISTRATIVE OFFICIALS

Office of the Secretary of State

Linda McCulloch, Secretary of State

Eric Stern, Chief Deputy Secretary of State

Jane Demaray, Deputy Secretary of State

Jorge Quintana, Chief Legal Counsel

Tana Gormely, Deputy for Business Services

Lisa Kimmet, Deputy for Elections & Government Services

Joe DeFilippis, Deputy for Records and Information Management

Laura Vachowski, Deputy for Administrative Rules and Notary Services

Brandi Pierson, Chief Financial Officer

For additional information concerning the Office of the Secretary of State,
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MONTANA LEGISLATIVE AUDIT DIVISION

FINANCIAL-COMPLIANCE AUDIT

Office of the Secretary of State

For the Two Fiscal Years Ended June 30, 2016

DECEMBER 2016

16-19

REPORT SUMMARY

The Office of the Secretary of State provides diverse services to Montana's voters, business community, and governmental agencies. These services include elections administration, administrative rule, corporate and Uniform Commercial Code filing, and records and information management. The office collected approximately \$5.3 million and \$6.3 million in revenue for services provided in fiscal years 2015 and 2016, respectively. This report does not contain any recommendations, but contains a qualified opinion on the office's financial schedules due to the effect of errors made in capitalizing the cost of the office's new computer system.

Context

Services provided by the Office of the Secretary of State (office) include maintaining the official records of the executive branch and the acts of the legislature; reviewing, maintaining, and distributing public-interest records of businesses and nonprofit organizations; filing administrative rules adopted by the state departments, boards, and agencies; filing and maintaining records of secured financial transactions, such as liens; and commissioning notaries public.

The office's main source of revenue is charges for services, derived from fees charged for corporate and Uniform Commercial Code (UCC) filings. Charges for Services revenue totaled \$5.3 million and \$6.3 million in fiscal years 2015 and 2016, respectively. Expenditures of the office totaled approximately \$7 million in each fiscal year. Personal services and operating expenses made up approximately 83 percent and 95 percent of total expenditures in fiscal years 2015 and 2016, respectively. Other significant expenditures in fiscal year 2015

included equipment expenditures related to recording construction work in progress for the office's new computer system.

Results

Our audit effort focused on significant revenue and expenditure activity including charges for services, personal services, and contracted services expenditures. We also reviewed transactions recording construction work in progress during the audit period. We audited this activity through sampling, analytical procedures, and testing the office's significant internal controls.

The report does not contain recommendations and we issued an unmodified opinion on five of the office's financial schedules for fiscal years 2015 and 2016. We issued a qualified opinion on the Schedule of Changes in Fund Equity for fiscal year 2015.

For a complete copy of the report (16-19) or for further information, contact the Legislative Audit Division at 406-444-3122; e-mail to lad@mt.gov; or check the web site at <http://leg.mt.gov/audit>

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Call toll-free 1-800-222-4446, or e-mail ladhotline@mt.gov.

Chapter I – Introduction

Introduction

We performed a financial-compliance audit of the Office of the Secretary of State (office) for the two fiscal years ended June 30, 2016. The objectives of this audit were to:

1. Determine whether the office's financial schedules present fairly, the financial position and results of operations of the office in accordance with state accounting policy for each of the two fiscal years ended June 30, 2016.
2. Obtain an understanding of the office's control systems to the extent necessary to support our audit of the office's financial schedules and, if appropriate, make recommendations for improvement in the management and internal controls of the office.
3. Determine whether the office has complied with selected laws and regulations.

During the audit we performed testing over significant activity including charges for services revenue, personal services, and contracted services expenditures. In addition, we reviewed significant transactions related to recording construction work in progress for the office's new computer system. We audited this activity through sampling and analytical procedures, as well as testing the office's significant internal controls. In addition to testing material activity, we completed testing over a variety of selected state laws. The audit report does not include any recommendations to the office.

Background

Article VI, Section 1, of the Montana Constitution authorizes the Secretary of State as an officer of the executive branch of state government. In fiscal year 2016, the office was authorized 57.75 full-time equivalent employees. The office includes the following five divisions.

- ◆ Elections and Government Services
- ◆ Administrative Rules of Montana and Notary Services
- ◆ Business Services
- ◆ Management Services
- ◆ Records and Information Management

Section 2-15-401, MCA, sets forth the Secretary of State's duties. The office provides a variety of services to the public in Montana. The office registers businesses and files documents for business entities operating in the state of Montana. It also files, stores, maintains, and preserves permanent records of the state. The office publishes

the Montana Administrative Register and the Administrative Rules of Montana. The office is also responsible for the commissioning of notaries public in Montana.

The Secretary of State also serves as chief election officer of the state, maintains uniformity in the application of the election laws and retains electronic records through the Elections and Government Services Division. In addition, the Secretary of State serves as a member of the Board of Land Commissioners, the Board of Examiners, and the Capital Finance Advisory Council.

Accounting Errors

During the audit, we evaluated the impact of errors related to Construction Work in Progress (CWIP) and the state's Other Post Employment Benefit (OPEB) liability. These errors resulted in a qualified opinion on the Schedule of Changes in Fund Equity for fiscal year 2015. The effect of these errors and subsequent corrections on the financial schedule are presented in the following table. This opinion can be found on page A-2 of the report.

Schedule of Changes in Fund Equity Fiscal Year 2015	
Enterprise Fund	Amount Overstated
FUND EQUITY: July 1, 2014	\$1,932,069
Direct Entries To Fund Equity	\$887,914
Prior Year Expenditures & Transfers-Out Adjustments	\$1,044,154

The following paragraphs describe these errors and the corrections made by the office.

Construction Work in Progress

The office recorded CWIP as required by state accounting policy for the development of the Secretary of State Information Management System (SIMS). CWIP was recorded prior to fiscal year 2015 for costs of developing the system since 2007. All CWIP was recorded in the Enterprise Fund; however, over half of the actual costs to develop the system were paid out of the Capital Project Fund. As a result, CWIP should have been recorded in the Capital Project Fund for costs paid out of that fund. This error resulted in July 1, 2014, fund equity in the Enterprise Fund to be overstated by approximately \$1.6 million. The related understatement of fund equity in the Capital Project Fund exists in the ledger that supports the state's Basic Financial Statements, and does not result in an error in the department's financial schedule included in this report.

This error was identified by management during the audit period. Entries were made to record the correct amount of CWIP in the Enterprise Fund and the Capital Projects Fund. To correct these errors in the Enterprise Fund, Direct Entries to Fund Equity and Prior Year Expenditures were recorded totaling approximately \$600,000 and \$1,000,000, respectively. We reviewed CWIP entries for fiscal years 2015 and 2016, and the entries were made correctly. Because the error was identified and corrected by management during the audit period, we make no recommendation.

Other Post Employment Benefit Liability

During the prior audit period, we determined that the state's OPEB liability and expenses were overstated since fiscal year 2007. The Department of Administration calculates and records the OPEB costs and the related liability for all state agencies. This error resulted in July 1, 2014, fund equity in the Enterprise Fund to be overstated by approximately \$300,000. In fiscal year 2015, the Department of Administration made correcting entries on behalf of the office to correct the overstatement. The correcting entries consisted of Direct Entries to Fund Equity totaling approximately \$300,000. While we were aware of this error during the last audit and communicated it to management, it was not significant enough in relation to total financial activity to result in an opinion qualification. During this audit, we had to consider the continuing effects of this error together with the CWIP error. When aggregated with the CWIP error, it is significant enough to contribute to the opinion qualification.

Independent Auditor's Report and Office Financial Schedules

LEGISLATIVE AUDIT DIVISION

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel



Deputy Legislative Auditors:
Cindy Jorgenson
Joe Murray

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

Introduction

We have audited the accompanying Schedules of Changes in Fund Equity, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Office of the Secretary of State for each of the fiscal years ended June 30, 2016, and 2015, and the related notes to the financial schedules.

Management's Responsibility for the Financial Schedules

Management is responsible for the preparation and fair presentation of these financial schedules in accordance with the regulatory format prescribed by the Legislative Audit Committee, based on the transactions posted to the state's accounting system without adjustment; this responsibility includes recording transactions in accordance with state accounting policy; and designing, implementing, and maintaining internal controls relevant to the preparation and fair presentation of the financial schedules that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial schedules based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial schedules. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial schedules, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the office's preparation and fair presentation of the financial schedules in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the office's internal control, and accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of

significant accounting estimates made by management, as well as the overall presentation of the financial schedules.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles

As described in Note 1, the financial schedules are prepared from the transactions posted to the state's primary accounting system without adjustment, in the regulatory format prescribed by the Legislative Audit Committee. This is a basis of accounting other than accounting principles generally accepted in the United States of America. The financial schedules are not intended to, and do not, report assets, liabilities, and cash flows.

The effects on the financial schedules of the variances between the regulatory basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinions on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed in the "Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles" paragraph, the financial schedules referred to above do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the office as of June 30, 2016, and June 30, 2015, or changes in financial position or cash flows for the years then ended.

Basis for Qualified Opinion on Regulatory Basis of Accounting

As described in Note 2, entries were made in fiscal year 2015 to correct errors related to the state's Other Post-Employment Benefit (OPEB) plan and Construction Work in Progress (CWIP) activity in fiscal years 2007 through 2014. These errors resulted in a misstatement to fund equity at July 1, 2014, in the Enterprise Fund. Correcting entries were made for both errors in fiscal year 2015, so June 30, 2015, fund equity is not affected. The correcting entries affected direct entries to fund equity and prior year expenditures. While these entries corrected the errors, direct entries to fund equity and prior year expenditures recorded were more than if the activity had been recorded correctly in prior periods, resulting in overstatements to both lines on the financial schedules. The effect of these errors and subsequent corrections are presented in the following table:

Schedule of Changes in Fund Equity Fiscal Year 2015	
Enterprise Fund	Amount Overstated
FUND EQUITY: July 1, 2014	\$1,932,069
Direct Entries To Fund Equity	\$887,914
Prior Year Expenditures & Transfers-Out Adjustments	\$1,044,154

Qualified Opinion on Regulatory Basis of Accounting

In our opinion, except for the effects of the matter described in the “Basis for Qualified Opinion on Regulatory Basis of Accounting” paragraph, the Schedule of Changes in Fund Equity for the fiscal year ended June 30, 2015, presents fairly, in all material respects, the results of operations and changes in fund equity of the Office of the Secretary of State in conformity with the basis of accounting described in Note 1.

Unmodified Opinions on Regulatory Basis of Accounting

In our opinion, the Schedule of Changes in Fund Equity for the fiscal year ended June 30, 2016, and the Schedules of Total Revenues & Transfers-In and Schedules of Total Expenditures & Transfers-Out for each of the fiscal years ended June 30, 2016, and 2015, present fairly, in all material respects, the results of operations and changes in fund equity of the Office of the Secretary of State in conformity with the basis of accounting described in Note 1.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 8, 2016, on our consideration of the Office of Secretary of State’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the office’s internal control over financial reporting and compliance.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

December 8, 2016

SECRETARY OF STATE'S OFFICE
SCHEDULE OF CHANGES IN FUND EQUITY
FOR THE FISCAL YEAR ENDED JUNE 30, 2016

	Federal Special Revenue Fund	Capital Projects Fund	Enterprise Fund
FUND EQUITY: July 1, 2015	\$ <u>518,889</u>	\$ <u>(1,750)</u>	\$ <u>(13,786)</u>
ADDITIONS			
Budgeted Revenues & Transfers-In	101,711		6,431,942
Nonbudgeted Revenues & Transfers-In	74		70,730
Prior Year Revenues & Transfers-In Adjustments			(1,681)
Direct Entries to Fund Equity	158	417,060	29
Total Additions	<u>101,943</u>	<u>417,060</u>	<u>6,501,021</u>
REDUCTIONS			
Budgeted Expenditures & Transfers-Out	211,862	418,155	6,455,041
Nonbudgeted Expenditures & Transfers-Out			45,167
Prior Year Expenditures & Transfers-Out Adjustments			39,860
Total Reductions	<u>211,862</u>	<u>418,155</u>	<u>6,540,067</u>
FUND EQUITY: June 30, 2016	\$ <u><u>408,969</u></u>	\$ <u><u>(2,845)</u></u>	\$ <u><u>(52,833)</u></u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE
SCHEDULE OF CHANGES IN FUND EQUITY
FOR THE FISCAL YEAR ENDED JUNE 30, 2015

	Federal Special Revenue Fund	Capital Projects Fund	Enterprise Fund
FUND EQUITY: July 1, 2014	\$ 623,960	\$ (172,957)	\$ 4,535,818
ADDITIONS			
Budgeted Revenues & Transfers-In	34,858		5,366,672
Nonbudgeted Revenues & Transfers-In	2		65,182
Prior Year Revenues & Transfers-In Adjustments			3,189
Direct Entries to Fund Equity		807,742	(3,246,895)
Total Additions	34,860	807,742	2,188,148
REDUCTIONS			
Budgeted Expenditures & Transfers-Out	139,932	636,535	5,872,971
Nonbudgeted Expenditures & Transfers-Out			36,368
Prior Year Expenditures & Transfers-Out Adjustments			828,413
Total Reductions	139,932	636,535	6,737,753
FUND EQUITY: June 30, 2015	\$ 518,889	\$ (1,750)	\$ (13,786)

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2016

	Federal Special Revenue Fund	Enterprise Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS			
Charges for Services		\$ 6,280,852	\$ 6,280,852
Investment Earnings	\$ 1,785	10,176	11,961
Sale of Documents, Merchandise and Property		91,185	91,185
Grants, Contracts, and Donations		70,057	70,057
Miscellaneous		48,721	48,721
Federal	100,000		100,000
Total Revenues & Transfers-In	101,785	6,500,992	6,602,776
Less: Nonbudgeted Revenues & Transfers-In	74	70,730	70,804
Prior Year Revenues & Transfers-In Adjustments		(1,681)	(1,681)
Actual Budgeted Revenues & Transfers-In	101,711	6,431,942	6,533,653
Estimated Revenues & Transfers-In	175,700	6,276,786	6,452,486
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ (73,989)	\$ 155,156	\$ 81,167
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS			
Charges for Services		\$ 109,679	\$ 109,679
Investment Earnings	\$ 1,011	5,593	6,604
Sale of Documents, Merchandise and Property		6,164	6,164
Miscellaneous		33,720	33,720
Federal	(75,000)		(75,000)
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ (73,989)	\$ 155,156	\$ 81,167

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE
SCHEDULE OF TOTAL REVENUES & TRANSFERS-IN
FOR THE FISCAL YEAR ENDED JUNE 30, 2015

	Federal Special Revenue Fund	Enterprise Fund	Total
TOTAL REVENUES & TRANSFERS-IN BY CLASS			
Charges for Services		\$ 5,269,708	\$ 5,269,708
Investment Earnings	\$ 1,824	3,478	5,302
Sale of Documents, Merchandise and Property		77,463	77,463
Grants, Contracts, and Donations		65,132	65,132
Miscellaneous		19,263	19,263
Federal	33,037		33,037
Total Revenues & Transfers-In	34,860	5,435,043	5,469,903
Less: Nonbudgeted Revenues & Transfers-In	2	65,182	65,184
Prior Year Revenues & Transfers-In Adjustments		3,189	3,189
Actual Budgeted Revenues & Transfers-In	34,858	5,366,672	5,401,530
Estimated Revenues & Transfers-In	26,000	4,905,130	4,931,130
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ 8,858	\$ 461,542	\$ 470,400
BUDGETED REVENUES & TRANSFERS-IN OVER (UNDER) ESTIMATED BY CLASS			
Charges for Services		\$ 454,524	\$ 454,524
Investment Earnings	\$ 822	(532)	289
Sale of Documents, Merchandise and Property		9,413	9,413
Miscellaneous		(1,863)	(1,863)
Federal	8,037		8,037
Budgeted Revenues & Transfers-In Over (Under) Estimated	\$ 8,858	\$ 461,542	\$ 470,400

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment.
Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2016

PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT	Business & Government Services	Total
Personal Services		
Salaries	\$ 3,106,118	\$ 3,106,118
Employee Benefits	881,883	881,883
Personal Services-Other	96,905	96,905
Total	<u>4,084,906</u>	<u>4,084,906</u>
Operating Expenses		
Other Services	1,153,709	1,153,709
Supplies & Materials	140,170	140,170
Communications	160,453	160,453
Travel	30,252	30,252
Rent	235,935	235,935
Utilities	5,397	5,397
Repair & Maintenance	20,618	20,618
Other Expenses	114,809	114,809
Goods Purchased For Resale	9,233	9,233
Total	<u>1,870,576</u>	<u>1,870,576</u>
Equipment & Intangible Assets		
Intangible Assets	805,240	805,240
Total	<u>805,240</u>	<u>805,240</u>
Post Employment Benefits		
Other Post Employment Benefits	159,367	159,367
Employer Pension Expense	249,995	249,995
Total	<u>409,362</u>	<u>409,362</u>
Total Expenditures & Transfers-Out	<u>\$ 7,170,084</u>	<u>\$ 7,170,084</u>
EXPENDITURES & TRANSFERS-OUT BY FUND		
Federal Special Revenue Fund	\$ 211,862	\$ 211,862
Capital Projects Fund	418,155	418,155
Enterprise Fund	6,540,067	6,540,067
Total Expenditures & Transfers-Out	7,170,084	7,170,084
Less: Nonbudgeted Expenditures & Transfers-Out	45,167	45,167
Prior Year Expenditures & Transfers-Out Adjustments	39,860	39,860
Actual Budgeted Expenditures & Transfers-Out	7,085,057	7,085,057
Budget Authority	10,161,365	10,161,365
Unspent Budget Authority	<u>\$ 3,076,307</u>	<u>\$ 3,076,307</u>
UNSPENT BUDGET AUTHORITY BY FUND		
Federal Special Revenue Fund	\$ 450,706	\$ 450,706
Capital Projects Fund	2,487,239	2,487,239
Enterprise Fund	138,362	138,362
Unspent Budget Authority	<u>\$ 3,076,307</u>	<u>\$ 3,076,307</u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

SECRETARY OF STATE'S OFFICE
SCHEDULE OF TOTAL EXPENDITURES & TRANSFERS-OUT
FOR THE FISCAL YEAR ENDED JUNE 30, 2015

	Business & Government Services	Total
PROGRAM (ORG) EXPENDITURES & TRANSFERS-OUT		
Personal Services		
Salaries	\$ 2,786,345	\$ 2,786,345
Employee Benefits	805,250	805,250
Personal Services-Other	32,287	32,287
Total	<u>3,623,883</u>	<u>3,623,883</u>
Operating Expenses		
Other Services	2,799,670	2,799,670
Supplies & Materials	110,722	110,722
Communications	184,631	184,631
Travel	34,062	34,062
Rent	218,657	218,657
Utilities	3,204	3,204
Repair & Maintenance	19,389	19,389
Other Expenses	94,076	94,076
Goods Purchased For Resale	17,889	17,889
Total	<u>3,482,301</u>	<u>3,482,301</u>
Grants		
From State Sources	8,548	8,548
From Federal Sources	2,372	2,372
Grant To Governmental Entities	50,269	50,269
Total	<u>61,189</u>	<u>61,189</u>
Debt Service		
Capital Leases	61	61
Total	<u>61</u>	<u>61</u>
Post Employment Benefits		
Other Post Employment Benefits	163,258	163,258
Employer Pension Expense	183,528	183,528
Total	<u>346,786</u>	<u>346,786</u>
Total Expenditures & Transfers-Out	<u>\$ 7,514,220</u>	<u>\$ 7,514,220</u>
EXPENDITURES & TRANSFERS-OUT BY FUND		
Federal Special Revenue Fund	\$ 139,932	\$ 139,932
Capital Projects Fund	636,535	636,535
Enterprise Fund	6,737,753	6,737,753
Total Expenditures & Transfers-Out	7,514,220	7,514,220
Less: Nonbudgeted Expenditures & Transfers-Out	36,368	36,368
Prior Year Expenditures & Transfers-Out Adjustments	828,413	828,413
Actual Budgeted Expenditures & Transfers-Out	6,649,438	6,649,438
Budget Authority	10,316,470	10,316,470
Unspent Budget Authority	<u>\$ 3,667,032</u>	<u>\$ 3,667,032</u>
UNSPENT BUDGET AUTHORITY BY FUND		
Federal Special Revenue Fund	\$ 580,484	\$ 580,484
Capital Projects Fund	2,905,394	2,905,394
Enterprise Fund	181,154	181,154
Unspent Budget Authority	<u>\$ 3,667,032</u>	<u>\$ 3,667,032</u>

This schedule is prepared from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) without adjustment. Additional information is provided in the notes to the financial schedules beginning on page A-11.

Montana Office of the Secretary of State

Notes to the Financial Schedules

For the Two Fiscal Years Ended June 30, 2016

1. Summary of Significant Accounting Policies

Basis of Accounting

The office uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental fund category (Federal Special Revenue and Capital Projects). In applying the modified accrual basis, the office records:

- ♦ Revenues when it receives cash or when receipts are realizable, measurable, earned, and available to pay current period liabilities.
- ♦ Expenditures for valid obligations when the office incurs the related liability and it is measurable, with the exception of the cost of employees' annual and sick leave. State accounting policy requires the office to record the cost of employees' annual and sick leave when used or paid.

The office uses accrual basis accounting for its Proprietary (Enterprise) fund category. Under the accrual basis, as defined by state accounting policy, the office records revenues in the accounting period when realizable, measurable, and earned, and records expenses in the period incurred when measurable.

Expenditures and expenses may include: entire budgeted service contracts even though the office receives the services in a subsequent fiscal year; goods ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end; and equipment ordered with a purchase order before fiscal year-end.

Basis of Presentation

The financial schedule format was adopted by the Legislative Audit Committee. The financial schedules are prepared from the transactions posted to the state's accounting system without adjustment.

The office uses the following funds:

Governmental Fund Category

- ♦ **Federal Special Revenue Fund** – to account for activities funded from federal revenue sources. Federal Special Revenue Fund includes activities related to the Help America Vote Act (HAVA), Election Reform Payments, and Election Assistance for Individuals with Disabilities.
- ♦ **Capital Projects Fund** – to account for financial resources used for the acquisition or construction of major capital facilities, other than those

financed by proprietary funds. The office uses this fund for activities related to the development of the Secretary of State Information Management System (SIMS).

Proprietary Fund Category

- ♦ **Enterprise Fund** – to account for operations (a) financed and operated in a manner similar to private business enterprises, where the Legislature intends that the department finance or recover costs primarily through user charges; (b) where the Legislature has decided that periodic determination of revenues earned, expenses incurred or net income is appropriate; (c) where the activity is financed solely by a pledge of the net revenues from fees and charges of the activity; or (d) when laws or regulations require that the activities' cost of providing services, including capital costs, be recovered with fees and charges rather than with taxes or similar revenues. The office Enterprise Fund includes Business Services, Administrative Rules and Notary Services, Elections, Executive Services, and Records and Information Management.

2. Direct Entries to Fund Equity

Direct entries to fund balances in the Federal Special Revenue, Capital Projects, and Enterprise funds include entries generated by SABHRS to reflect the flow of resources within individual funds shared by separate agencies, corrections of errors that occurred at least two fiscal years prior, change in accounting principle or a change in the application of an accounting principle, or retroactive change mandated by the GASB in conjunction with the implementation of a pronouncement.

In FY16, the Direct entry of \$158 to fund equity in the Federal Special Revenue Fund was the result of an error correction that occurred at least two fiscal years prior. The error correction was related to the FY2012 4% Accommodation Tax.

The Direct entries to fund balances in the Capital Projects fund are made at each fiscal year-end as part of the fiscal year-end cash closing process to reflect the flow of resources within individual funds shared by separate agencies.

In FY15, Direct entries to fund equity in the Enterprise fund were made to correct an error related to Governmental Accounting Standards Board (GASB) Statement 45- Accounting and Financial Reporting by Employers for Postemployment Benefits other than Pensions and a retroactive change mandated by GASB in conjunction with the implementation of Statement 68- Accounting and Financial Reporting for Pensions.

- ♦ The state's OPEB is limited to post-employment health care benefits to employees and dependents that elect to continue coverage after retirement and pay administratively established premiums. The Department of Administration (DOA) calculates and records the OPEB costs and the related liability on an annual basis for all state agencies. Generally accepted

accounting principles (GAAP) and state policy require the calculation to include an adjustment be made to offset the amount of interest already included in the actuarial estimates. DOA believed the adjustment applied only if the state made contributions to fund the liability. However, the adjustment is not optional. The restatement related to adjustment for GASB 45 resulted in an increase to fund equity of \$282,693.84.

- ♦ The retroactive change in accounting principle for GASB 68 resulted in a net decrease to fund equity in the amount of \$2,914,376.43.

In FY15, Direct entries to fund equity in the Enterprise Fund include adjustments in order to correct errors related to Construction Work in Progress (CWIP) entries from previous periods that occurred at least two fiscal years prior. The CWIP is related to the development of the Secretary of State Information Management System (SIMS). The purpose of these direct fund equity entries was to accurately record CWIP in both the Enterprise and Capital Projects fund. The result of these corrections was a decrease in fund equity of \$605,211.98.

3. Unspent Budget Authority

The Schedule of Total Expenditures & Transfers-Out presents unspent budget authority for the Capital Projects Fund in the amount of \$2,905,394 for fiscal year 2015 and \$2,487,239 for fiscal year 2016. The unspent authority relates to the implementation of a new Secretary of State Information Management System which will replace an aging and outdated legacy mainframe application that contains information on every registered business in Montana, and several smaller applications and databases that support office accounting and other filings. Unspent budget authority for capital projects in the beginning of a project is not unusual as projects typically span over multiple fiscal years. As a result, the unspent authority rolls forward to the next fiscal year.

Report on Internal Control and Compliance

LEGISLATIVE AUDIT DIVISION

B-1

Angus Maciver, Legislative Auditor
Deborah F. Butler, Legal Counsel



Deputy Legislative Auditors:
Cindy Jorgenson
Joe Murray

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL SCHEDULES PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

The Legislative Audit Committee
of the Montana State Legislature:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the Schedules of Changes in Fund Equity, Schedules of Total Revenues & Transfers-In, and Schedules of Total Expenditures & Transfers-Out of the Office of the Secretary of State for each of the fiscal years ended June 30, 2016, and 2015, and the related notes to the financial schedules, and have issued our report thereon dated December 8, 2016. Our report includes a qualified opinion on the Schedule of Changes in Fund Equity for the fiscal year ended June 30, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial schedules, we considered the Office of the Secretary of State's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial schedules, but not for the purpose of expressing an opinion on the effectiveness of Office of the Secretary of State's internal control. Accordingly, we do not express an opinion on the effectiveness of the Office of the Secretary of State's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial schedules will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal controls was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Office of the Secretary of State's financial schedules are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination on financial schedule amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the office's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the office's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Respectfully submitted,

/s/ Cindy Jorgenson

Cindy Jorgenson, CPA
Deputy Legislative Auditor
Helena, MT

December 8, 2016

OFFICE OF THE
SECRETARY OF STATE

OFFICE RESPONSE



MONTANA SECRETARY OF STATE

LINDA McCULLOCH

December 20, 2016

Angus Maciver
Legislative Auditor
State Capitol
Helena, MT 59620-1705

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DEC 20 2016
LEGISLATIVE AUDIT DIV.

Dear Angus Maciver, Legislative Auditor

I am extremely proud of this report, my final fiscal audit from the Legislative Audit Division.

It has taken a considerable amount of effort and commitment from the staff of the Secretary of State Office to accomplish their goal of a report with no recommendations. I'd like to take this opportunity to recognize Brandi Pierson, CFO, her fiscal staff as well as the staff in the Secretary of State Office for the excellent job they do.

Thank you to you and your staff for the professional work and interactions with our SOS Staff during this fiscal audit process. During my 16 years working with the Legislative Audit Division I have enjoyed the expertise and experience they represent.

If we can provide additional information, please contact us.

Sincerely,

A handwritten signature in cursive script that reads "Linda McCulloch".

Linda McCulloch
Secretary of State